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January 24, 2005

VIA HAND DELIVERY

Mr. Charles Terreni  
Chief Clerk of the Commission  
SC Public Service Commission  
P. O. Drawer 11649  
Columbia, SC 29211

RE: Application of Bush River Utilities, Inc., for approval of a  
New Schedule of Rates and Charges for Sewage Service provided  
to Residential and Commercial Customers in all areas served.  
Docket No.: 2004-259-S  
Development Service Inc. Rate Case Legal Professional Services  
PSC Docket No.: 2004-212-S ---- Our File No.: 6550

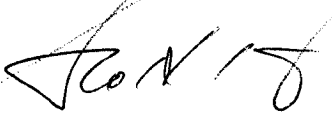
Dear Mr. Terreni:

Enclosed please find the original and one copy (1) of the **Order Ruling on Application for Rate Increase** filed on behalf of Development Service, Inc. in the above referenced docket. By copy of this letter, I am serving all parties of record.

If you have questions or need additional information, please do not hesitate to contact me.

Sincerely,

Elliott & Elliott, P.A.



Scott Elliott

SE/jcl

Enclosures

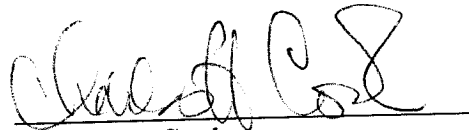
c: All parties of records w/enc.

## CERTIFICATE OF SERVICE

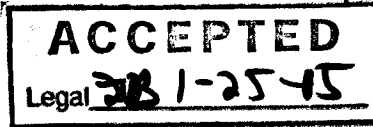
The undersigned employee of Elliott & Elliott, P.A. does hereby certify that she has served below listed parties with a copy of the Order Ruling on Application for Rate Increase on behalf of Development Service, Inc., indicated below by hand delivery on the date indicated below:

RE: Application of Development Service, Inc., for approval of new schedule of rates and charges for sewage service provided to residential and commercial customers in all areas served.  
Docket No. 2004-212-S

PARTIES SERVED: Florence P. Belser, Esquire  
General Counsel  
1441 Main Street  
Suite 300  
Columbia, SC 29201

  
Charles H. Cook

January 24, 2005



**ORIGINAL**

**BEFORE**

**THE PUBLIC SERVICE COMMISSION** 24 JUL 2007

**OF SOUTH CAROLINA**

**DOCKET NO. 2004-212-S**

IN RE: Application of Development Service, Inc. for Approval  
of New Schedule of Rates and Charges for Sewerage  
Service Provided to Residential and Commercial  
Customers in all areas Served.

) **ORDER**  
) **RULING ON**  
) **APPLICATION**  
) **FOR INCREASE**  
) **IN RATES**

## **I. INTRODUCTION**

This matter is before the Public Service Commission of South Carolina (the "Commission") on the Application of Development Service, Inc. ("DSI" or the "Company"), filed on July 28, 2004, seeking approval of a new schedule of rates and charges for sewer service that DSI provides to its customers within its authorized service area in Lexington County, South Carolina. The Application was filed pursuant to S.C. Code Ann. Section 58-5-210 *et seq.* (1976), as amended, and 26 S.C. Code Regs. 103-821 (1976).

By letter dated August 6, 2004, the Commission's Executive Director instructed DSI to publish a prepared Notice of Filing, one time, in newspapers of general circulation in the areas affected by DSI's Application. The Notice of Filing indicated the nature of the Application and advised all interested persons desiring to participate in the scheduled proceedings of the manner and time in which to file appropriate pleadings for inclusion in the proceedings. In the letter of August 6, 2004, the Executive Director also instructed DSI to notify directly, by U.S. Mail, each customer affected by the Application by mailing each customer a copy of the Notice of Filing. DSI furnished the Commission

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with an Affidavit of Publication demonstrating that the Notice of Filing had been duly published and with a letter in which DSI certified that it had complied with the instruction of the Executive Director to mail a copy of the Notice of Filing to all customers affected by the Application.

On January 5, 2005, a public hearing concerning the matters asserted in DSI's Application was held in the Commission's hearing room located at Synergy Business Park, 101 Executive Center Drive – Saluda Building, Columbia, South Carolina. During the proceedings, DSI was represented by Scott Elliott, Esquire and Charles H. Cook, Esquire. The Office of Regulatory Staff was represented by Florence P. Belser, Esquire and Shannon Hudson, Esquire. There were no intervenors or public witnesses.

At the hearing, DSI presented the testimony of Keith G. Parnell, President and Operations Manager of DSI. The ORS Staff presented the testimony of Dawn M. Hipp, Sharon Scott and Willie J. Morgan, Auditors for the Office of Regulatory Staff.

In considering the Application of DSI, the Commission must consider competing interests. The interests of the consumers to receive quality service and a quality product at a reasonable rate compete with the interests of the provider to have the opportunity to earn a fair rate of return. Regulation, as it has developed in the United States, is concerned with rates, service, [and] safety .... Charles F. Phillips, Jr., *The Regulation of Public Utilities*, (1993) at 171. Rate regulation has two aspects: control of the rate level (earnings) and control of the rate structure (prices). *Id.* As to the rate level, public utilities are entitled to cover all allowable operating costs and to have the opportunity to earn a "fair" rate of return. *Id.* Collectively, these items comprise a company's total revenue requirements. *Id.* As to the rate structure, public utilities are permitted to establish rates

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that, at a minimum, will cover their revenue requirements. *Id.* at 171-72. Such rates must be “just and reasonable,” with no “undue” discrimination. *Id.* at 172.

Thus, in considering the Application of DSI, the Commission must give due consideration to DSI’s total revenue requirements, comprised of allowable operating costs and the opportunity to earn a fair return. To this end, the Commission will review the operating revenues and operating expenses of DSI and will endeavor to establish adequate and reasonable levels of revenues and expenses. Further, the Commission will consider a fair return for DSI based upon the record before it. Should the Commission’s determination show that rates should be increased, the Commission will then design rates that will meet the revenue requirements of DSI but that are also just and reasonable and free of undue discrimination.

## **II. FINDINGS OF FACT**

1. DSI is a sewer utility providing sewer service in its assigned service area within South Carolina, and its operations in South Carolina are subject to the jurisdiction of the Commission, pursuant to S.C. Code Ann. § 58-5-10, *et seq.* (1976), as amended.

2. The appropriate test year period for the purposes of this proceeding is the twelve-month period ending December 31, 2003.

3. The Commission will use operating margin as a guide in determining the lawfulness of the Company’s rates and in the fixing of just and reasonable rates.

4. By its Application, DSI is seeking a two stage increase in its rates and charges for sewer service which results in additional revenues of \$100,833 after the first stage of the rate increase and additional revenues of \$146,839 after the second stage.

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5. The appropriate operating revenues for DSI for the test year, based upon rates in effect pursuant to Order #96-44, indicates a negative income before taxes of (\$2,146).

6. The appropriate operating expenses for DSI for the test year are \$250,029.

7. The operating margin for the test year is (8.65)%.

8. Based on the operating margin for the test year we find that DSI has demonstrated the need for an increase in rates.

9. When applied to test year operations, the rates requested and proposed by DSI result in an operating margin of 2.87% during the first stage increase and 5.75% for the second stage increase.

10. The Commission finds that an operating margin of 2.87% after the first stage increase and an operating margin of 5.75% after the second stage increase are fair and reasonable for a utility the size of DSI. The Commission further finds that in order to lessen the impact of a one-time rate increase that it is appropriate to phase-in the rate increase.

11. The Commission finds that the rate increase should be phased-in in two stages, the first stage increase to be effective immediately and the second stage increase to be effective upon a showing to this Commission that the construction of the wastewater treatment facility upgrade to Bush River Utilities, Inc. (Bush River) has been completed to the satisfaction of South Carolina Department of Health and Environment Control (DHEC) and at a cost of not less than \$932,278.

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12. To achieve an ultimate operating margin of 5.75% following a two stage phase-in of rates, the Commission approves the increase of rates and operating margins as reflected in Exhibit 2 of the application of DSI.

13. In order for DSI to have the opportunity to earn the herein approved operating margins under the phase-in of the rates, DSI must be allowed the necessary additional revenues under the first part of the phase-in and additional revenues under the second part of the phase-in, all as reflected by the application and exhibits of DSI.

14. The appropriate operating margin for DSI based upon the herein approved adjustments and rates is 2.87% for the first part of the phase-in and 5.75% for the second part of the phase-in.

15. The Commission finds that DSI should begin maintaining its books and records in accordance with the NARUC Uniform System of Accounts for Class C Sewer Utilities, as adopted herein by this Commission.

### **III. EVIDENCE TO JUSTIFY FINDINGS OF FACT**

In this section, the Commission sets forth the evidence relied upon in making its Findings of Fact as set forth in Section II of this Order.

#### **1. EVIDENCE FOR FINDING OF FACT NO. 1**

This finding is uncontested by the Parties.

#### **2. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2**

The evidence supporting this finding, that the appropriate test year period for the purposes of this proceeding is the twelve-month period ending December 31, 2003, is contained in the Application filed by DSI and in the testimony and exhibits of the parties' witnesses.

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A fundamental principle of the ratemaking process is the establishment of a test year period. In *Heater of Seabrook v. Public Service Commission of South Carolina*, 324 S.C. 56, 478 S.E.2d 826 (1996), the Supreme Court of South Carolina noted that “[t]he ‘test year’ concept is very important in the rate-setting process. In order to determine what a utility’s expenses and revenues are for purposes of determining the reasonableness of a rate, one must select a ‘test year’ for the measurement of the expenses and revenues.” 478 S.E.2d 828 n.1 (1996). The test year is established to provide a basis for making the most accurate forecast of the utility’s rate base, reserves, and expenses in the near future when the prescribed rates are in effect. *Porter v. South Carolina Public Service Commission*, 328 S.C. 222, 493 S.E.2d 92 (1997), citing *Hamm v. S.C. Pub. Serv. Comm’n*, 309 S.C. 282, 422 S.E.2d 110 (1992). The test year provides a basis upon which a commission staff will conduct its audit of a company’s books. Phillips, *The Regulation of Public Utilities* at 196. For rate-making purposes, only just and reasonable expenses are allowed; only used and useful property (with certain exceptions) is permitted in the rate base. *Id.* The commission must have a basis for estimating future revenue requirements. *Id.*

The Commission concludes that the appropriate test year to use in the instant proceeding is the twelve-month period ending December 31, 2003. No party contested the use of that test year as proposed by DSI in its Application. To the contrary, all witnesses relied upon that test year period in presenting their evidence.

### 3. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3



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In its Application, DSI did not specify or propose a particular rate setting methodology. However, in its Application, DSI did identify net depreciable property consisting of utility plant and equipment of \$125,266. Application, Exhibit 3.

“The Public Service Commission has wide latitude to determine an appropriate rate-setting methodology.” *Heater of Seabrook v. Public Serv. Comm’n of South Carolina*, 324 S.C. 56, 64, 478 S.E. 2d 826, 830 (1996). South Carolina law does not require the Commission to use any particular price-setting methodology. *Id.* S. C. Code Ann. Section 58-5-240 (H) (Supp. 2003) directs the Commission to specify an allowable operating margin in all water and wastewater orders. However, “that directive does not mean that the operating margin methodology must be used in determining a fair rate of return.” *Id.* Operating margin “is less appropriate for utilities that have large rate bases and need to earn a rate of return sufficient to obtain the necessary equity and debt capital that a larger utility needs for sound operation.” *Id.* According to the Application, DSI’s per books total rate base, or net depreciable property, is \$125,266. Application, Exhibit 3.

Accordingly, DSI has not presented evidence of a rate base of sufficient size on which to utilize return on rate base as a price setting methodology, the Commission finds that operating margin is the appropriate rate-setting methodology to use in this case.

#### 4. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

We find Keith G. Parnell and C. Ken Parnell to be credible witnesses. DSI operates as a collection only sewer provider. Its sister company, Bush River Utilities, Inc. provides the treatment for DSI’s effluent. According to ORS witness Scott, DSI’s treatment cost paid to Bush River constitutes 75% of DSI’s revenues. Bush River by consent order with DHEC must close its lagoon and construct a new wastewater

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treatment facility at a minimum cost of \$932,278. DHEC has approved construction of Bush River's treatment plant upgrade. DSI, Bush River, and Midlands Utility, Inc. all owned by Keith G. Parnell and C. Ken Parnell have applied by and obtained financing sufficient to pay for Bush River's upgrade.

The Application of DSI indicates that it is seeking additional revenues for the first stage of the proposed rates for its sewer operations and additional revenue for the second stage increase to pay the expected increase in operating costs as a result of the construction of the Bush River upgrade and to cure the now negative operating margin reflected in the test year.

#### 5. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

DSI's Application shows per book test year total operating revenues of \$247,883. Application, Exhibit 2. While the ORS reaches a different revenue figure, we find the Applicant's calculations to be credible.

#### 6. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

The Application reflects operation expenses of \$250,029 for the test year. Applicant worked closely with the ORS, to include lengthy on site inspection and thorough discovery. In spite of the justification provided to ORS, the agency fails to accept DSI's test year expenses to be known and measurable. This Commission finds that DSI has justified these expenses, was reasonable and prudent in its operations and that its operation expenses in the test year are known and measurable.

The Commission is guided in its decision by the case of *Heater of Seabrook, Inc. v. Public Service Commission of South Carolina*, 324 S.C. 56, 478 S.E.2d 826 (1996), in which the Supreme Court of South Carolina stated "[w]hen calculating expenses in rate

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cases, Commission should use only test year data and known and measurable changes occurring after the test year.”

However certain accounting issues remain.

First with respect to rate case expenses, the Commission approves DSI’s rate case expenses submitted which include \$24,949.59 in legal fees and costs submitted as Exhibit 15 and further approves the amortization period of three years proposed by DSI. The Commission finds that rate case expenses are a proper item for inclusion in rates. Ideally, the amortization period for the recovery of the rate case expenses should allow for recovery of those expenses between rate cases. However, it is impossible to foresee what the future holds and to state with any certainty when the Company may need to return to this Commission for rate adjustment.

In *Hamm v. South Carolina Public Service Commission*, 309 S.C. 282, 422 S.E.2d 110 (1992), the Supreme Court of South Carolina stated

Adjustments for known and measurable changes in expenses may be necessary in order that the resulting rates reflect the actual rate base, net operating income, and cost of capital. The adjustments are within the discretion of the Commission and must be known and measurable within a degree of reasonable certainty. Absolute precision, however, is not required.

(citing *Michaelson v. New England Tel. & Tel. Co.*, 121 R.I. 722, 404 A.2d 799 (1979)).

While the Commission cannot state with absolute precision when the Company will return for another rate proceeding, the Commission must provide a sufficient amortization period under which DSI may recover its expenses. The Commission finds a three year amortization period reasonable.

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Second, DSI proposes to depreciate plant over 20 years and equipment of 7 years. ORS Staff did not accept DSI's proposed adjustment to depreciation expense.

The Commission finds that DSI properly reflected the proposed depreciation expense for both stages of expenses on current property. In particular, the severe duty expected of the plant and equipment, the continuously evolving nature of regulation and the resulting obsolete the useful life of plant and equipment. DSI has made an adequate showing through the testimony and exhibits of Keith Parnell and Ken Parnell in this docket as well as that in Docket 2004-259-S that its schedule of depreciation of 20 years for plant and 7 years for equipment is appropriate. This Commission will exercise its authority to accept the depreciation schedules proposed by DSI in this action.

#### 7. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The operating margin for the test year under present rates and after accounting and pro forma adjustments approved herein is a negative (8.65)%. Even the ORS witnesses testified as to the negative operating margin for the test year from its findings.

#### 8. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT 8

Based upon finding of Fact 7, the Commission finds that DSI has demonstrated a need for rate relief in the form of rate increase. The ORS concedes that the Applicant is entitled to a one stage rate increase based on a proposed operating margin of 14.92%. However DSI has persuaded the Commission that it is indeed entitled to a two stage rate increase. As set out earlier, Bush River treats the effluent collected by DSI. The ORS concedes that 75% of DSI's revenues are paid to Bush River for wastewater treatment expenses. DSI has no other alternative provider. By consent order with DHEC, Bush River has agreed to close its wastewater lagoon and build a modern wastewater treatment facility. Bush

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River is acting under the compulsion of the DHEC order enforceable by criminal and civil penalties. Moreover, Keith and Ken Parnell, owners of DSI and Bush River have gone to great lengths to comply with the DHEC consent order. First, Bush River has designed a wastewater treatment plant upgrade which has been approved by DHEC. The minimum cost of the system is \$932,278. Bush River and DSI have both applied for and obtained financing sufficient to pay for the construction of the wastewater upgrade. Not only have Bush River and DSI pledged their assets to pay for the loan but also Keith and Ken Parnell have similarly committed their personal assets. While the ORS protests that the upgrade cost are not known and measurable, the Commission is forced to the conclusion that the need for the upgrade, the proposal to build the upgrade, the financing obtained to construct the upgrade, the necessity of compliance with the consent order, and the good faith efforts of both Keith and Ken Parnell are all known and measurable. Any concern by the ORS that the two stage rate increase, once granted, may not prove to be necessary can be met by this Commission by requiring DSI and Bush River to satisfy this Commission that the upgrades were built in accordance with the plans submitted to this Commission and at the cost submitted to this Commission prior to the implementation of the second rate increase. Set out hereafter, both conditions will be made a part of this order.

#### 9. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT 9

When applied to test year operations, the rates requested and proposed by DSI result in an operating margin of 2.87% during the first stage increase and 5.75% for the second stage increase requested.

#### 10. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT 10

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The Commission finds that the approved operating margins are certainly reasonable for a utility the size of DSI. Accordingly, in order to lessen the impact to the customers of a one time rate increase, the Commission further finds that it is appropriate to phase-in the rate increase. The Commission recognizes that DSI faces increased costs in continuing to serve its customers. DSI requires substantial increased revenues just to meet day-to-day operations, without considering the costs associated with the expected increase in operating costs and the necessary capital improvements required on the system for its provider Bush River. The Commission would note, that for DSI to meet these increases costs in a single rate increase as urged by the ORS, its operating margin would have to exceed 26% given the adjustments proposed by the ORS.

The Commission acts out of concern for the customers. The Commission recognizes that the customers are being requested to pay a sizeable rate for sewer service. However, implementing the rate increase in two stages prevents the need for a second rate case with its considerable attendant costs and relieves the financial strain on its customers. The utility is operating in the negative. Without an influx of revenues, the viability of DSI could certainly be in question. The Commission must allow for the utility to be viable in order to provide the services to the public.

DSI has demonstrated a need for the rate increase without considering the fact that DSI is facing increased operating costs in order to meet DHEC's requirements. As evidenced by the testimony of DSI's president, Mr. Parnell, DSI has obtained a loan in order to finance the capital projects needed to meet DHEC's requirements. Thus, the Commission must consider that DSI will need to show financial viability and an ability to repay debt in order to obtain necessary financing for the capital projects. However, while

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keeping in mind the financial status and viability of DSI, the Commission does not ignore the impact of rate increases on the public. As a policy matter, the Commission concludes that it must devise a rate plan which will provide needed revenues to DSI but also lessen the impact of the increase on the customers. To balance these competing interests, the Commission determines that a phase-in of the rate increase is appropriate.

A phase-in of rates is not a new concept in South Carolina. A phase-in of rates was involved in the case of *Hamm v. South Carolina Public Service Commission*, 294 S.C. 320, 364 S.E. 2d 455 (1988), when South Carolina Electric & Gas Company brought the V.C. Summer Nuclear Station into rate base. While DSI's rates are being set using operating margin methodology rather than rate of return methodology, the large one-time rate increase would be the same for the customers regardless of the methodology used to set the rates. Therefore, the Commission finds that the public interest requires a phase-in of this rate increase in order to lessen the impact of the rate increase on the customers.

#### 11. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT 11

According to the record, Bush River and DSI has explored the possibility of a tie-in with the City of Columbia and West Columbia sewer system. However, neither city has the capacity for service to Bush River and DSI. Thus, it appears Bush River and DSI have no present alternative but to construct a new wastewater treatment plant. DSI will certainly benefit from Bush River's improvement to its system. However, DSI as a result will incur additional operating costs as Bush River must increase its rates to pay for an expensive upgrade. As for the amounts of the phase-in of the rates, we approve the increase requested by DSI.

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The first stage increase will be implemented immediately upon issuance of this order. The second stage rate increase must not be implemented until DSI files with this Commission a report detailing the construction of the upgrades and proof of compliance with all DHEC requirements concerning the upgrade. This report must be filed with the Commission and served on ORS. The report required before implementing the second stage of the rate increase shall detail to the Commission: (1) the completion of the upgrades; (2) the costs expended on the upgrades; and (3) any other issues which the Commission may order DSI to address in the report.

#### 12. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

The Commission must design rates which will allow DSI to improve its financial position by moving from an operating margin of (8.65)% to an ultimate operating margin of 5.75% following a two part phase-in of rates. To achieve an ultimate operating margin of 5.75% following the second stage of rate increases, the Commission accepts and adopts the rates proposed by DSI.

#### 13. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

Using the Operating Revenues and Operating Expenses approved herein, the Commission is able to calculate the income requirement for the utility associated with the herein approved phase-in of rates. Operating Margin is achieved by dividing net operating income for return minus interest expense by total operating revenues. Thus the revenue requirement for DSI under operating margin methodology found appropriate in this Order and using the operating revenues and operating expenses approved herein is calculated as \$348,716 for the opportunity to achieve the 2.87% operating margin found



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reasonable for the first stage of new rates; and \$394,722 for the opportunity to achieve the 5.75% operating margin found reasonable for the second stage of the rate increase.

In order for DSI to achieve the requisite income requirement to have the opportunity to earn the herein approved operating margins under the phase-in of the rates, DSI must be allowed additional revenues of \$100,833 under the first part of the phase-in; additional revenues of \$146,839 under the second part of the phase-in.

#### 14. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 14

S.C. Code Ann. Section 5-240(H) (Supp. 2003) provides, in part, that “[t]he [C]ommission shall specify an allowable operating margin in all water and wastewater orders.” Based upon the operating margins approved herein for the phase-in of rates and the revenues and expenses also approved herein, the corresponding operating margins for the phase-in of rates is calculated to be 2.87% for the first stage of the rate increase, and 5.75% for the second stage of the rate increase.

#### 15. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT 15

The Commission finds that DSI should begin maintaining its books and records in accordance with the NARUC Uniform System of Accounts for Class C Sewer Utilities, and as adopted by this Commission herein. We find that DSI should maintain its books and records using the NARUC Uniform System of Accounts as required by 26 S.C. Code Regs. 103-517 (Supp. 2003). Further, we advise DSI to consult with the Staff if guidance is needed concerning the requirements of the NARUC Uniform System of Accounts.

### IV. CONCLUSIONS OF LAW

Based upon the Findings of Fact as contained herein and the record of the instant proceeding, the Commission makes the following Conclusions of Law:

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1. Operating margin is the appropriate guide for the Commission to use in determining the lawfulness of the rates of DSI and in fixing of just and reasonable rates for DIS to charge its customers in South Carolina.
  2. A fair operating margin for the sewer operations of DSI in South Carolina is 2.87% following the first stage of the rate increase; and 5.75% following the second stage of the rate increase.
  3. For the test year of December 31, 2003, the appropriate operating revenues, under present rates, are \$247,883, and the appropriate operating expenses, under present rates and as adjusted in this Order, are \$250,029.
  4. Using the operating margins found to be fair and reasonable in this Order, the revenue requirements for DSI are \$348,716 after the first stage of the rate increase; and \$394,722 after the second stage of the rate increase.
  5. In order for DSI to have an opportunity to earn the operating margins found reasonable and approved in this Order and to meet the revenue requirements, DSI must be allowed additional revenues of \$100,833 under the first stage of the rate increase; and additional revenues of \$146,839 under the second stage of the rate increase.
  6. The rates approved in this Order are designed to be just and reasonable without undue discrimination and are also designed to meet the revenue requirements of the Company.
  7. Based on the increase in rates approved herein, the appropriate operating margins for DSI on its South Carolina operations are 2.87% for the first phase, and 5.75% for the second phase.

IT IS THEREFORE ORDERED THAT:

BY ORDER OF THE COMMISSION: